DC-2 Exam Review:
Tips and Traps

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Question Types

- ALL TRUE EXCEPT: Find one FALSE answer (A, B, C, D, E)
- Which are TRUE: Find ALL TRUE answers (I, II, III)

Test Tips

- RTFD!!!! Watch for double negatives!
- Okay to write on the test – use the space for calculations.
- Check limits – probably 2014 amounts.
- Check answers from the bottom to the top.
- Answer all questions but skip hard ones and go back.
- Remember – you can miss 15 to 20 questions ☺

What We Will NOT Cover in Today's Webcast

- 401(k) Safe harbor contributions – know SH match and QNEC rules, what SH covers (TH, ADP versus ACP), notices, EACA, QACA
- Fee disclosure and 404(c)
- QDIA
- Code of Conduct

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What We Will NOT Cover in Today's Webcast

- 401(k) testing
- Contributions
- Allocations – including cross-tested
- Distributions

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401(k) Plans: Contributions

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Who Is the Employer?

What retirement plans are available?

Entity	SEP	SIMPLE	Non-401(k) qualified	401(k)	403(b)	457
Sole proprietor	Yes	Yes	Yes	Yes	No	No
Partnership	Yes	Yes	Yes	Yes	No	No
LLC	Yes	Yes	Yes	Yes	No	No
Corporation (C-Corp or Sub-S)	Yes	Yes	Yes	Yes	No	No
Public school, college or university	Yes	Yes	Yes	Yes	Yes	No
Tax-exempt	Yes	Yes	Yes	Yes	Maybe	No*
Governmental	Yes	Yes	Yes	No	No	Yes

*Tax exempt entities (except churches) generally can adopt 457 plans, but they are "unfunded" "top hat" non-qualified plans which may benefit only highly compensated management employees.

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Plan Operation Overview

Employees

- Eligibility
- Enrollment
- Auto-enrollment
- Terminate, leave of absence

"Money in"

- Deferral, match, employer
- Payroll and fund Elections
- Recordkeeping, statements
- Rollovers, transfers

"Money out"

- Termination
- Death, disability
- Retirement
- Loans, hardships

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Plan Operation Overview

Ongoing reporting

- Recordkeeping: on demand options
- Participant statements
- Investment review

Annual reporting

- Form 5500, audit
- Summary Annual Report
- Plan valuation summary
- Notices: QDIA, safe harbor, fee disclosure

Compliance

- Non-discrimination testing
- Coverage testing
- Contribution limits
- Top heavy

Contributions

401(k) Plan

- **Deferrals (EE)**
- **Catch-up deferrals (EE)**
- **Roth deferrals (EE)**
- **After-tax employee (EE)**
- Matching (ER)
- Safe harbor, top heavy (ER)
- Discretionary profit sharing (ER)
- Gateway (cross-tested) (ER)
- QNEC, QMAC (ER)
- Rollover (not counted toward limits) (EE)

Contributions in RED can be matched by the employer.
Deferrals and Roth limited to 402g limit of $18,00 in 2015.
Catch-up contributions are $6,000 in 2015.
Max overall contribution limit (415): $53,000 or $58,000

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401(k) Rules

401(k) Deferrals

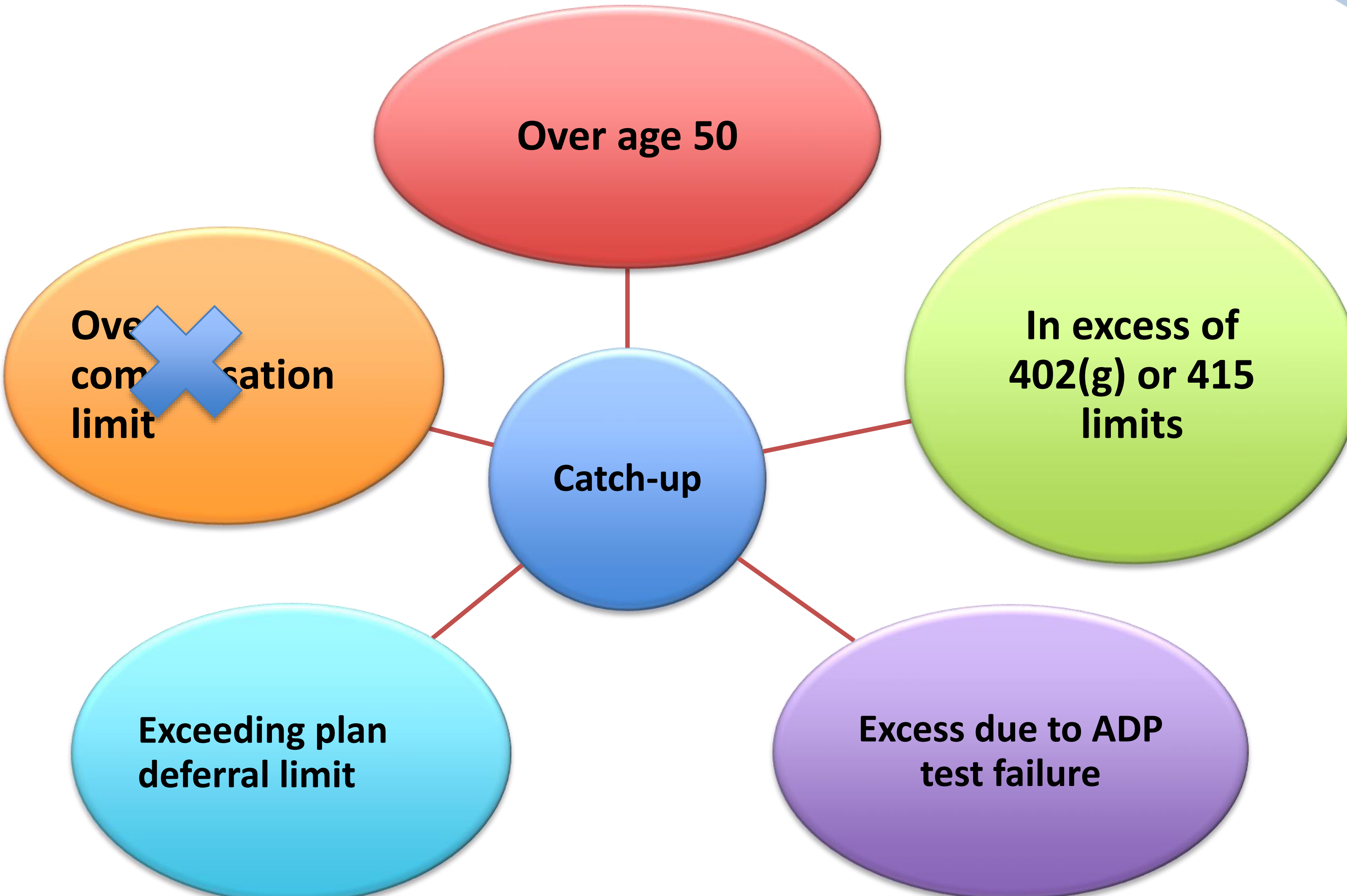
- Elected by employee from paycheck PRIOR to pay being “currently available”
- Limited to dollar amount for the CALENDAR YEAR (employee’s tax year)
- ALL 401(k) plan deferrals count toward limit
- Can elect pre-tax or Roth (after-tax with tax-free earnings)
- Designated Roth deferrals are tax-free on distribution assuming they are “qualified” (five years of “seasoning”)
- Over 50 years of age can defer more, “catch-up contribution,” which can include Roth
- Subject to social security and FUTA taxes

401(k) Rules

401(k) Deferrals in Multiple Plans

- Limited to 402g amount for the CALENDAR YEAR (employee's tax year) in ALL plans
- Excess (plus earnings) can (and should) be distributed
- Participant responsibility and participant choice
- 401(a)(30) is a PLAN and EMPLOYER limit

401(k) Contributions



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Question 56

All of the following statements regarding 401(k) plans are TRUE, EXCEPT:

A. An employee may make an election to defer compensation that is currently available.
B. Participants may have their deferral rates automatically increased with future pay increases.
C. After-tax employee contributions may be found in a 401(k) plan.
D. Elective contributions are subject to withholding of Social Security and Medicare taxes.
E. A partner may make a deferral election on compensation that is received as draw.

Question 58

All of the following statements regarding designated Roth contributions are TRUE, EXCEPT:

A. Designated Roth contributions are elective contributions made on an after-tax basis.
B. Designated Roth contributions are subject to the IRC §402(g) limit.
C. Designated Roth contributions are tested for nondiscrimination purposes in the ADP test.
D. Designated Roth contributions may not be re-characterized as catch-up contributions.
E. Designated Roth contributions are not subject to taxation when distributed from a qualified plan.

Question 59

All of the following statements regarding 401(k) plans are TRUE, EXCEPT:

A. Safe harbor 401(k) contributions may not be distributed on account of an active participant's financial hardship.
B. A rural cooperative may adopt a new 401(k) plan.
C. The plan may require two years of service for eligibility in the employer matching contribution component of the plan.
D. Local governmental employers may adopt a new 401(k) plan.
E. The plan may not condition the allocation of a QNEC upon whether the employee made elective contributions.

Question 61

All of the following may be considered catch-up contributions, EXCEPT:

A. Elective contributions exceeding the IRC §402(g) dollar limit.
B. Elective contributions exceeding the plan's compensation limit.
C. Elective contributions exceeding a plan-imposed contribution limit.
D. Elective contributions exceeding the IRC §415 annual addition limit.
E. Elective contributions exceeding the amount allowed to satisfy the ADP test.

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Question 62

All of the following statements regarding excess deferrals made by a single participant to two unrelated employers' 401(k) plans are TRUE, EXCEPT:

- The participant did not exceed the IRC §402(g) limit in either plan.
- Total deferrals for the participant were $30,000.

A. Elective deferrals made under one employer's plan are taken into account to determine whether the other employer's plan has violated the IRC §401(a)(30) limit.
B. Excess deferrals are includible in gross income for tax purposes.
C. Excess deferrals may be corrected by distribution of the excess amount.
D. It is the participant's responsibility to request timely distributions of excess deferrals from the applicable plan(s).
E. The participant may choose which plan or plans to take distributions from to correct the excess deferrals.

401(k) Plans: Allocations

Allocation Formulas

- Pro-rata based on 414(s) compensation
- Fixed dollar amount for all employees based on service NOT more than one week
- Dollar or percentage for NHCEs only
- Integrated with social security (permitted disparity under 401(l))
- Age-weighted*
- Service/compensation points*
- Cross-tested*
- Top heavy and/or safe harbor contributions may also be required as additional contributions.

Does not satisfy design-based safe harbor and is subject to IRC 401(a)(4) testing.

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Non-Discriminatory Integrated Allocations

Taxable Wage Base (TWB) = weighted toward NHCEs

Use TWB at beginning of the plan year – not prorated

Maximum excess disparity is 5.7 percent

Allows HCEs (comp > TWB) to get higher contribution

Also known as permitted disparity

Maximum excess percentage up to two times base percent

Integration level can be percentage or dollar

Integration level can equal TWB or be a percentage of TWB

100% of TWB = 5.7%

80% of TWB = 5.4%

60% of TWB=4.3%

Hybrid Plan: Cross-Tested Design

401(k) new comparability

$52,000/

$57,500 max

RTFD!

Demographics and Family Members Matter!

Test usually based on age

Gateway = Lesser of five percent of one-third of highest HCE percentage

Hybrid Plan: Cross-Tested Design

401(k) new comparability

Employer can set contribution annually for each group

NOT a design-based safe harbor allocation; subject to testing

Plan document specifies how contributions are allocated within a group

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401(a)(4) Non-Discrimination Test

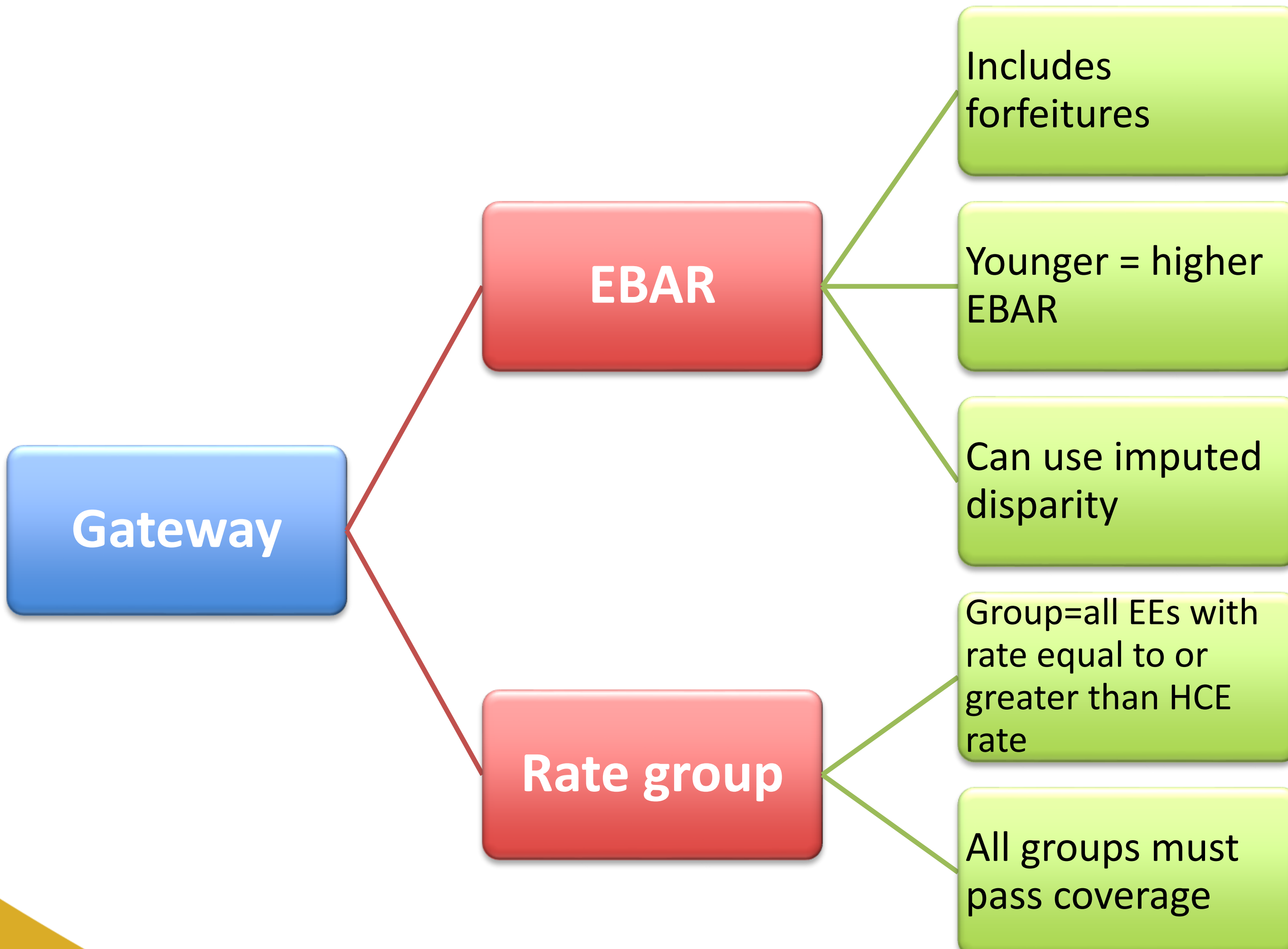
Gateway (five percent or one-third of top HCE percentage)

ABT (Average Benefits Test)

ABPT (Average Benefits Percentage Test)

"Cross tested" means DB plans test on contributions OR DC plans testing on benefits. Plan can satisfy the test based on benefits OR contributions. Plans with older employees benefit from benefits-based testing.

401(a)(4) Nondiscrimination Test



Question 8

All of the following statements regarding nondiscrimination testing are TRUE, EXCEPT:

A. Plans may satisfy the general test on the basis of either contributions or benefits.
B. A defined benefit plan that satisfies nondiscrimination on a contributions basis is said to be cross-tested.
C. A defined contribution plan must first satisfy gateway requirements before it can be cross-tested.
D. A rate group consists of an HCE and all other participants who have an allocation rate equal to or less than the HCE's allocation rate.
E. Non-elective forfeiture allocations are included when determining rate groups.

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Question 20

All of the following are design-based safe harbor allocation formulas, EXCEPT:

A. An employer contribution of $5 per week of service in the plan year.
B. Pro rata allocation based on points for service and compensation.
C. An allocation using permitted disparity under IRC §401(l).
D. An employer contribution of 50¢ for every hour of service during the plan year.
E. An allocation of $1,000 per participant for NHCEs only.

Question 21
All of the following are design-based safe harbor allocation formulas, EXCEPT:

A. Pro rata based on IRC §414(s) compensation.
B. Allocation of $150 per participant.
C. An employer contribution of $10 per month of service in the plan year.
D. An employer contribution of $5 for every hour of service during the plan year.
E. Allocation using permitted disparity under IRC §401(l).

Question 22

Which of the following statements regarding new comparability plans is/are TRUE?

I. A new comparability plan gives the employer the discretion to determine the annual contribution level for each allocation group.
II. A new comparability plan gives the employer the discretion over the manner in which contributions are allocated within each allocation group.
III. New comparability formulas meet safe harbor requirements and need not use general testing to satisfy nondiscrimination requirements.

A. I only
B. II only
C. I and III only
D. II and III only
E. I, II and III

Question 24

All of the following statements regarding benefits-based testing are TRUE, EXCEPT:

A. If two participants receive the same percentage of compensation as a contribution allocation, the younger participant will have a higher EBAR.
B. Only one rate group needs to satisfy the coverage rules of IRC §410(b).
C. A participant's EBAR may be adjusted for imputed disparity.
D. Benefits-based testing generally favors older employees.
E. A defined contribution plan must first satisfy gateway requirements before it can be cross-tested.

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Question 25

Based on the following information, determine the members of Participant B's rate group for general testing under IRC §401(a)(4):

Participant	Status	Allocation Rate
A	HCE	11%
B	HCE	9%
C	HCE	5%
D	NHCE	15%
E	NHCE	9%
F	NHCE	3%

A. Participants B and E only
B. Participants B, D and E only
C. Participants A, B, D and E only
D. Participants A, B, C, D and E only
E. Participants A, B, C, D, E and F

Question 27

Based on the following information, determine the allocation to Participant A:

- The Taxable Wage Base (TWB) is $113,700.
- The integration level is 85% of the TWB.
- Participant A's compensation for the plan year is $150,000.
- The employer has elected to make a contribution of 4% plus 4% on excess compensation.

A. $4,548.00
B. $4,737.00
C. $6,000.00
D. $6,640.80
E. $8,134.20

Integ Level	$113,700.00	85.00%	$96,645.00
Base	$150,000.00	4.00%	$6,000.00
Excess*	$53,355.00	4.00%	$2,134.20
ALLOCATION			$8,134.20
***Total comp - comp>integ level**			

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Question 28

Which of the following statements regarding permitted disparity under the IRC §401(l) safe harbor is/are TRUE?

I. The integration level for participants who enter mid-year is prorated.
II. The integration level may be stated as a percentage, up to 100% of the TWB in effect for the plan year.
III. The integration level may be stated as a dollar amount, up to the TWB in effect for the plan year.

A. I only
B. II only
C. I and III only
D. II and III only
E. I, II and III

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Question 35

All of the following are valid permitted disparity formulas, EXCEPT:

□ The integration level for the plan is 60% of the TWB in effect for the plan year.

A. 3.0% of total compensation plus 3.0% of compensation in excess of the integration level.
B. 4.0% of total compensation plus 4.0% of compensation in excess of the integration level.
C. 5.0% of total compensation plus 5.0% of compensation in excess of the integration level.
D. 5.4% of total compensation plus 4.3% of compensation in excess of the integration level.
E. 7.0% of total compensation plus 4.3% of compensation in excess of the integration level.

401(k) Plans: Distributions Part 1

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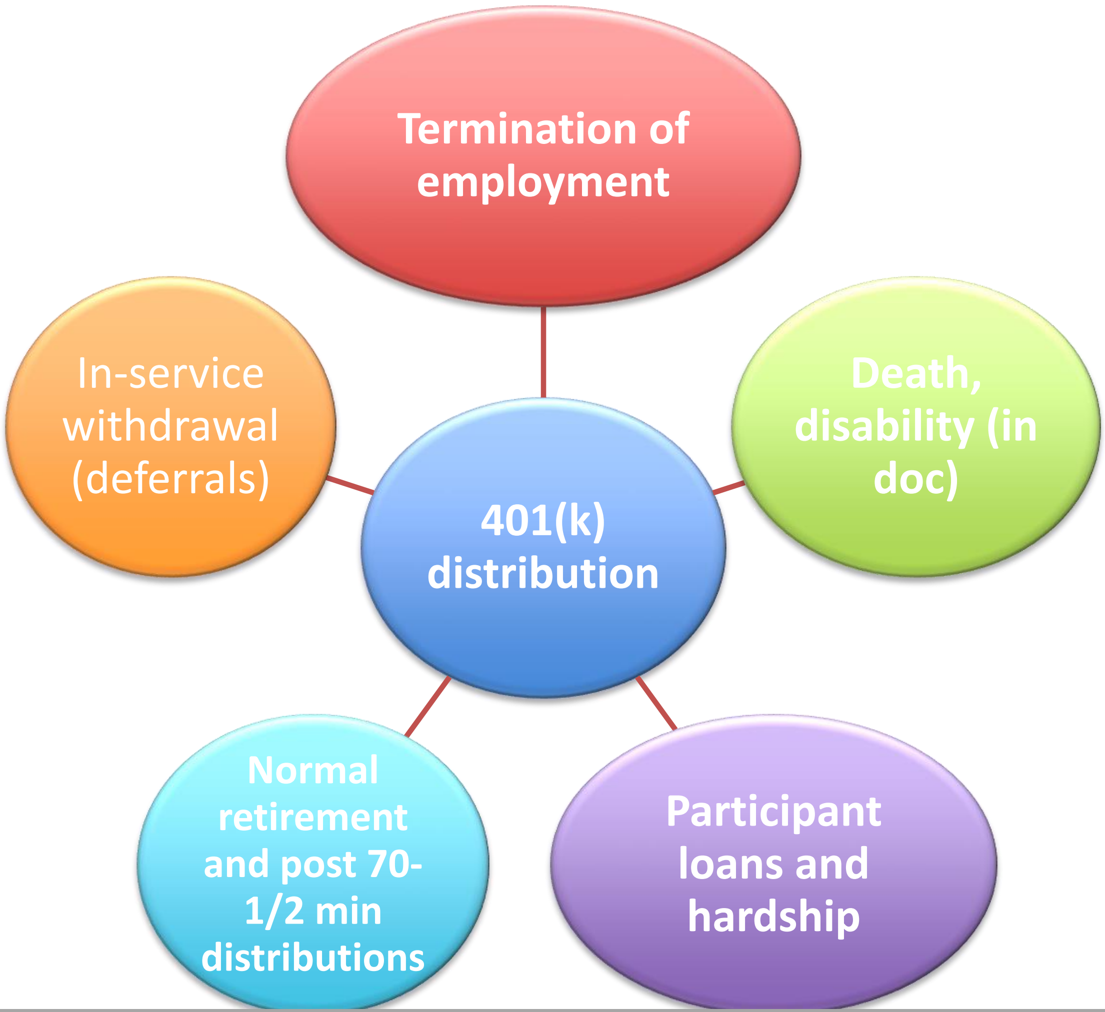
Distributions: Events



In general, distributions are taxable (except Roth and loans repaid timely) unless they are rolled over or transferred to an IRA or another qualified plan.

Distributions: Overview

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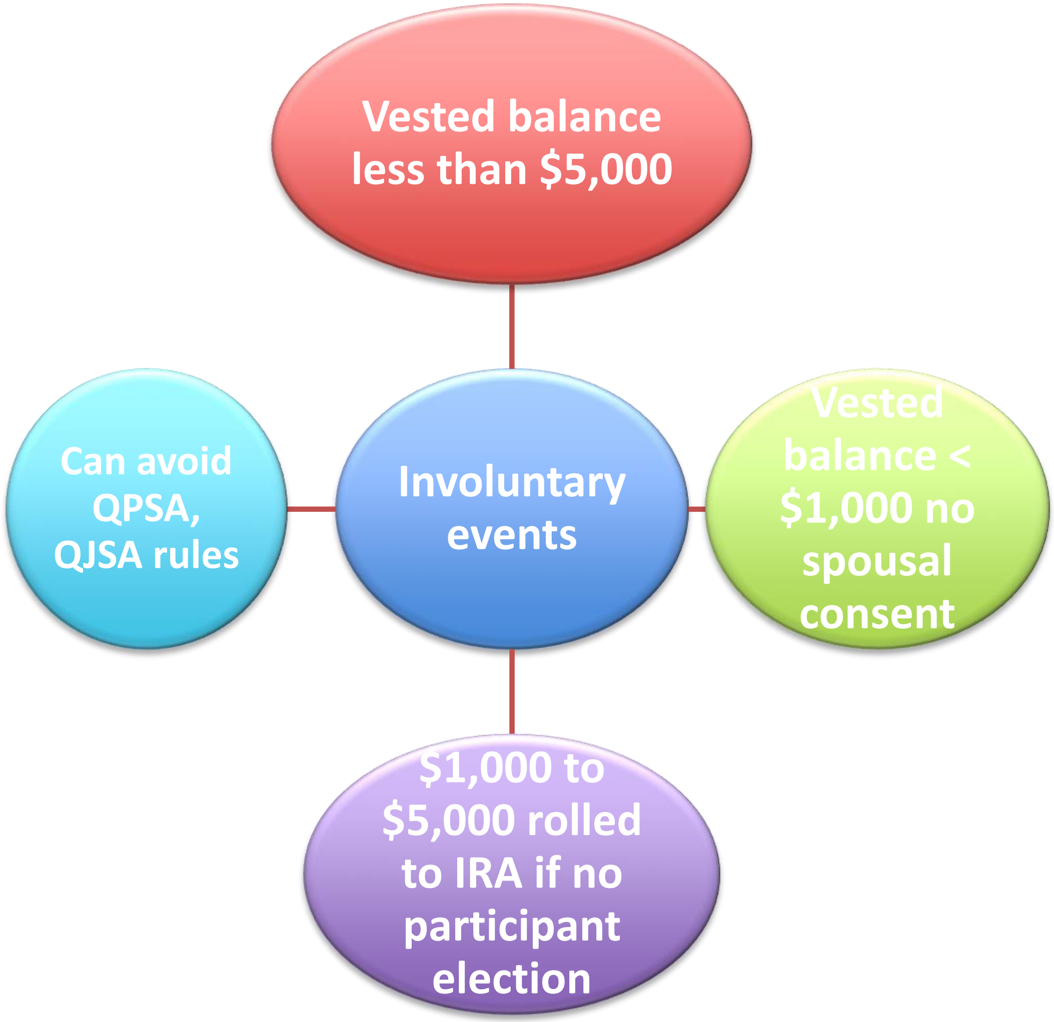
Distributions: Involuntary



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Spousal Consent Requirements

Termination of employment distribution greater than $5,000

Not required for distributions <$1,000; only tax notice

Spousal Consent

Non-Annuity distribution (QJSA docs only)

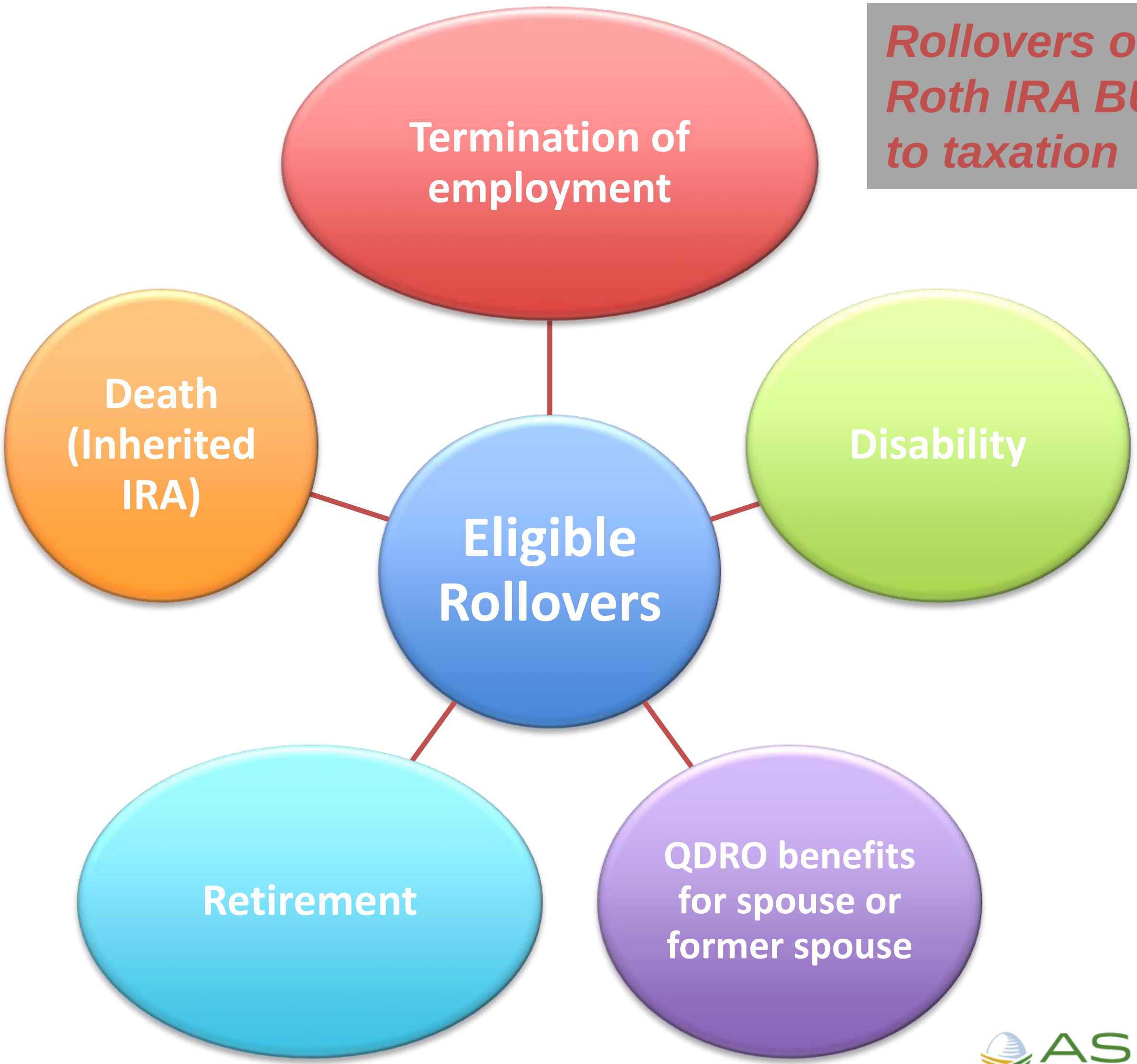
Retirement, death, disability, in-service distribution

Non-spouse beneficiary designation

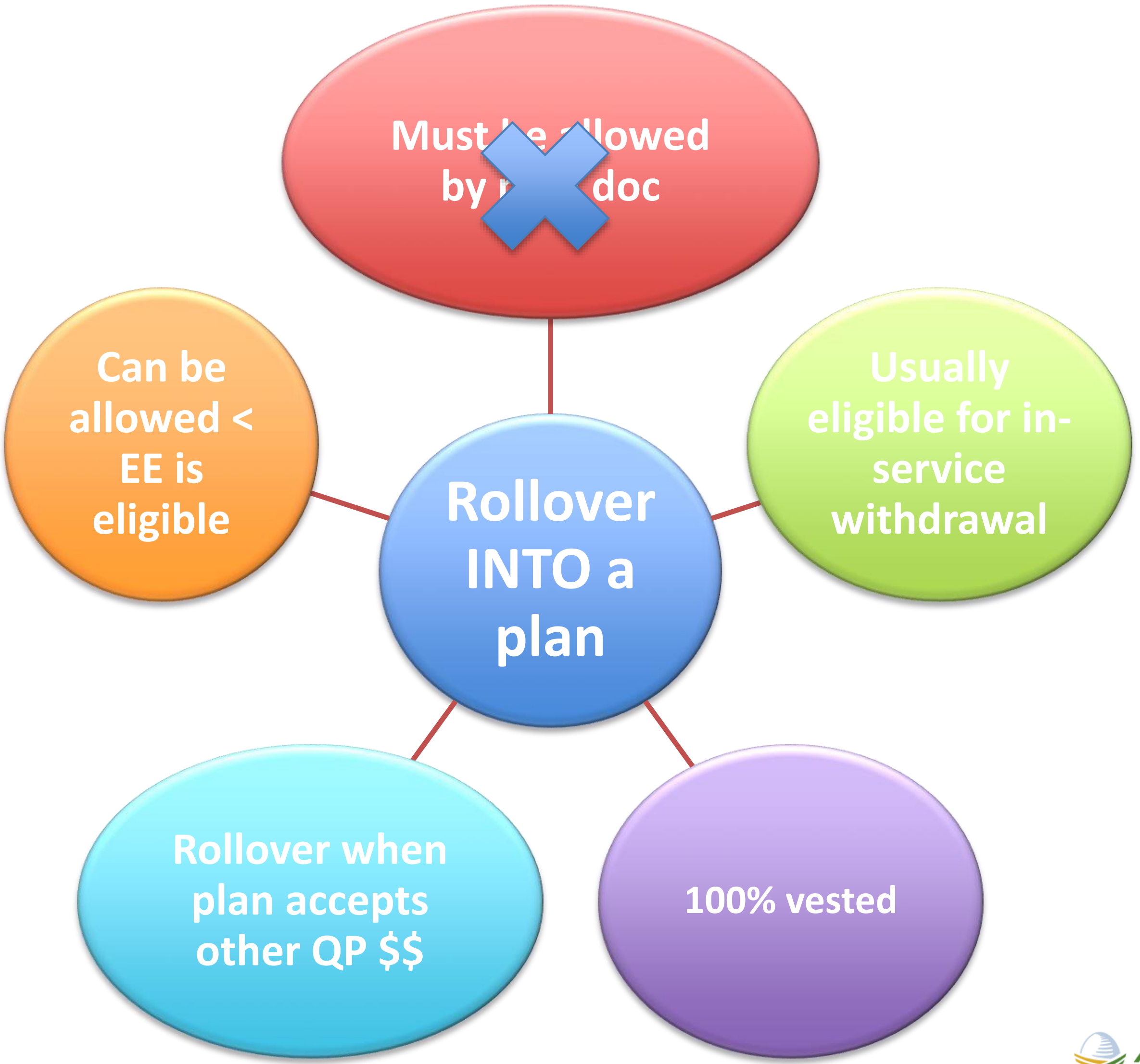
Participant loans and hardship

Distributions: Rollovers

Rollovers okay into Roth IRA BUT subject to taxation



Rollovers



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Early Distributions

Subject to ten percent excise tax prior to age 59-1/2	NOT subject to ten percent excise tax
• Lump-sum distribution • Unpaid loan balances • Hardship withdrawals • In-service withdrawal • Plan termination	• Death, disability • Substantially equal payments over life of participant • Termination of service after age 55 • Pay deductible medical expenses • Loans repaid timely • Rollovers and direct transfers • After age 59-1/2 • Qualifying Roth distribution • QDRO distribution to alternate payee • Corrective distributions

In service withdrawals are not permitted from money purchase plans prior to NRA.

Qualified Joint and Survivor Annuity (QJSA)

Required in DB, MPP and target plans

OPTIONAL: 401(k) and PSP plans unless transferred assets from pension plan

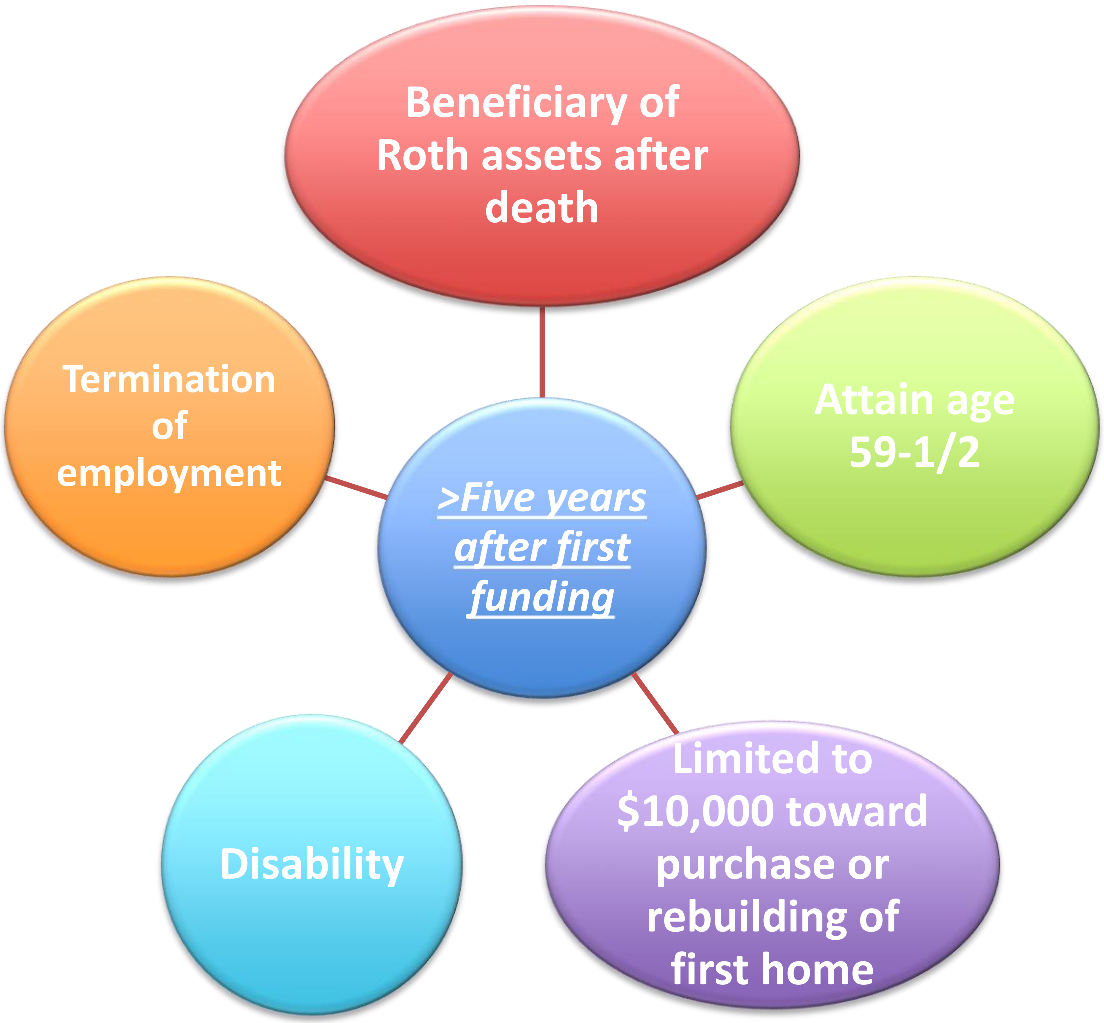
Married participants can take a different form of distribution with spousal consent

Participants must receive notice and election forms for QJSA prior to distribution

QJSA is a minimum of 50% survivor benefit; QJSA for unmarried EE is single life annuity

Distribution Notices

Qualified Roth Distributions



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Required Minimum Distributions

Rules

- Amount based on life expectancy table
- Must take into account all balances subject to minimum distribution (includes IRAs)
- ***By April 1st following year attain age 70-1/2 OR retirement year if still working and not >5% owner***
- Second and subsequent distributions due by 12/31
- NOT eligible for rollover
- OPTIONAL withholding but no election = ten percent

Penalties

- Participant is responsible for amount and timing of distribution (not adviser)
- Cannot take credit for higher than required distribution and apply it to future year
- Plan is responsible for paying distribution – if failure, have to file with IRS, pay filing fees and penalties
- ***Participant taking late distribution pays 50 percent excise tax***

RMD Calculation

Determine RBD

Five percent owner or NOT?

Life only factor versus J&S factor

Balance as of PREVIOUS year end

Watch out for April 1st dates!

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Question 2

Based on the following information, determine the required beginning date for an RMD to Participant A:

- Participant A is a 10% owner.
- Participant A was born on July 10, 1942.
- Participant A is still employed as of December 31, 2013.

A. April 1 following the year of separation from service.
B. December 31 following the year of separation from service.
C. April 1, 2013.
D. December 31, 2013.
E. April 1, 2014.

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Question 11

Which of the following statements regarding withholding is/are TRUE?

I. If all distributions to the participant for the calendar year are less than $200, no tax withholding is required.
II. An RMD is subject to the 20% mandatory withholding because it is an eligible rollover distribution.
III. If a direct distribution includes noncash assets, applicable withholding must be made from the cash portion of the distribution.

A. I only
B. II only
C. I and III only
D. II and III only
E. I, II and III

Question 12

All of the following statements regarding distribution reporting are TRUE, EXCEPT:

A. Form 945 must be filed each year, even if there was no withholding liability.
B. The amount of federal tax income withheld from a distribution is reported on Form 1099-R.
C. Form 945 reconciles actual deposits with withholding liability.
D. If part of a distribution is directly rolled over and the other part is paid to the participant, two Form 1099-Rs must be prepared.
E. Distributions from governmental 457(b) plans are reported on Form 1099-R.

Question 13

All of the following distributions are exempt from the 10 percent tax on early distributions, EXCEPT:

A. Payments made to a participant’s beneficiary after a participant dies.
B. A distribution attributable to a participant’s disability.
C. A distribution made to a participant, age 50 who has elected early retirement under the plan.
D. Corrective distributions of excess deferrals under IRC §402(g).
E. A distribution made to an alternate payee pursuant to a QDRO.

Question 17

All of the following statements regarding eligible rollover distributions are TRUE, EXCEPT:

A. A hardship withdrawal from a qualified plan is not eligible for rollover.
B. Qualified plans are required to accept rollover contributions.
C. A rollover option may be available to the surviving spouse of a deceased participant.
D. A QDRO payment to a former spouse may be eligible for rollover.
E. A rollover option is not available on all distributions.

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Question 18

Based on the following information, determine the amount of the RMD:

- The participant's required beginning date is April 1, 2014.
- The participant's account balance as of 12/31/12 was $345,000.
- The participant's account balance as of 12/31/13 was $379,000.
- The life expectancy factor under the uniform lifetime table is 25.6.
- The life expectancy factor under the joint and last survivor table is 30.
- The sole beneficiary is the participant's spouse who is 15 years younger than the participant.

A. $11,500.00
B. $12,633.33
C. $13,018.87
D. $14,804.69
E. $23,000.00

1. Check the RBD – will tell you which plan year to start with.
2. RMD is for 12/31/13, but you look at PRIOR PYE balance – as of 12/31/12.
3. Find the correct expectancy factor – use J&S factor of 30 because spouse > 10 yrs younger than participant
4. $345K/30 = $11,500

Question 19

All of the following statements regarding distributions are TRUE, EXCEPT:

A. A partial distribution is usually elected in a single sum.
B. In a defined contribution plan, the lump sum is the value of the vested account balance.
C. The period of time over which installment distributions can be made may be based on life expectancy.
D. A defined contribution plan may make payments as an annuity directly from the participant’s account.
E. An installment payment may be for a specific dollar amount each year, with the remaining account balance distributed at the end of the payment term.

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Question 23

Which of the following statements regarding rollover distributions is/are TRUE?

I. A rollover IRA may be used as a conduit to transfer distributions from one qualified plan to another.
II. Rollover to a traditional IRA delays the taxation of the amount rolled over.
III. Defined contribution plan funds that are eligible for rollover may be directly rolled over into Roth IRAs even if they are not designated Roth contributions.

A. I only
B. II only
C. I and III only
D. II and III only
E. I, II, and III

Question 33

All of the following statements regarding QJSAs are TRUE, EXCEPT:

A. A joint and 50% survivor annuity provides the surviving spouse a payment equal to 50% of the participant’s payment.
B. A QJSA for an unmarried participant is payable to the participant’s beneficiary.
C. A joint and 100% survivor annuity provides the surviving spouse a payment equal to 100% of the participant’s payment.
D. SEPs are exempt from the QJSA requirements.
E. SIMPLE IRAs are exempt from the QJSA requirements.

Question 63

All of the following statements regarding proper distribution of 401(k) elective contributions are TRUE, EXCEPT:

A. A participant may borrow against his accumulated elective contributions.
B. Elective contributions may be withdrawn as in-service distributions provided that the employee has completed five years of plan participation.
C. A participant may elect to receive his elective contributions upon termination of employment.
D. A participant may be entitled to receive in-service distributions of his elective contributions after attaining age 591/2.
E. Elective contributions may be rolled over into an IRA when eligible for distribution.

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401(k) Plans: Distributions Part 2

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Qualified Domestic Relations Order (QDRO)

QDROs must specify a distribution type allowed in the document.

Can name former spouse, child, other dependents as alternate payee

Must specify percentage of account balance to alternate payee

Participant and alternate payee must be notified in writing if DRO Is QDRO and procedures for QDRO

Participant and alternate payee must be notified of receipt of the DRO

Must have a <u>distributable event</u> before alternate payee can receive $$

Qualified Domestic Relations Order (QDRO)

- State judgment or decree under state domestic relations law
- Must include names and last know mailing addresses of participant and alternate payee(s)
- Must include plan name
- Must include percent of benefits to be paid to alternate payee
- Must include number of payments or period to which the order applies

Non-401(k) Hardship Rules

- Plan document defines financial circumstances for hardship
- Only permitted in certain circumstances, e.g., immediate and heavy financial need due to unexpected event
- Subject to pre-59-1/2 10% penalty
- PSP can be limited to vested account balance

401(k) Hardship Withdrawals

Rules

Deferral contributions = amount of proven hardship need + estimated tax

Deferrals must be suspended for six months and spousal consent required

Taxation

Taxable as income – reported on 1099

10% early distribution penalty

Must first take all other currently available distributions under the plan, including loans (unless that would increase the participant's hardship).

401(k) General Hardship Rules

Events Test

- Hardship can be immediate and heavy even if foreseeable or voluntarily incurred
- Plan sponsor determination based on relevant facts and circumstances

Needs Test

- Resources include spouse's and minor children's
- Must obtain plan loan first if it will not increase the hardship

Unlike safe harbor hardship rules, participant statement of hardship is not enough. The plan sponsor has an administrative burden to make a reasonable determination of the hardship.

401(k) Safe Harbor Hardship

Hardship Withdrawals: Immediate and Heavy Financial Need for Participant OR Dependents

- Unreimbursed medical expenses
- Down payment on principal residence
- Tuition and fees for higher education (next 12 months)
- Eviction or foreclosure on primary residence
- Expenses for repair of damages to principal residence
- Funeral expenses

The IRS safe harbor hardship rules DO NOT require a participant to provide a written statement that the need cannot be met by any other means or to provide financial records.

Participant Loans (Exempt from PT Rules)

Limits	50% of account balance up to $50,000	Must be non-discriminatory and equally available to HCEs and NHCEs
Repayment	Principal and interest repaid at least quarterly over no more than five years*	Interest rate must be reasonable
Default and suspension	Loan payments can be suspended for approved leaves of absence, e.g., military service	Loan defaults are treated as taxable distributions to the employee

Unless secured by principal residence

Loans must be permitted by the plan document and loans must be made according to the terms of the plan loan policy and/or the loan terms in the plan document.

Loan Policy Requirements

Type of collateral if necessary

Basis on which loans are approved or denied

Identity or position of person administering loan program

Loan limits

Loans Under IRC 72(p)

The second set of rules is found in IRC §72(p). Generally, distributions from a qualified plan are considered taxable income to the recipient. IRC §72(p) provides an exception to this general rule, under which a loan will not be considered to be taxable income. Under the IRC rules, a loan is not income if:

- The amount of the loan is within the legal limits.
- The term of the loan does not exceed legal limits.
- The repayment schedule for the loan meets the IRC requirements.
- The loan is actually repaid according to the loan terms.

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Loans Under IRC 72(p)

IRC §72(p) provides that loans may be considered "deemed distributions" if they are not repaid according to loan terms. However:

- The amount of the loan is currently taxable to the participant.
- The "deemed" distribution is NOT actually distributed.
- The loan obligation still exists after a deemed distribution.
- Repayments to a deemed distribution load are considered after-tax contributions when the account is eventually distributed.

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Multiple Loan Calculation

Determine date

50% of vested balance (includes loans)

Subtract outstanding loan balance within LAST 12 MONTHS

Plan must allow for multiple loans

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Question 3
Which of the following statements regarding participant loan refinancing is/are TRUE?

I. The replaced loan is considered repaid after the refinancing transaction is completed.
II. Only one loan may be replaced during a refinancing transaction.
III. The interest rate on the replaced loan is used when determining the terms of the replacement loan.

A. I only
B. II only
C. I and III only
D. II and III only
E. I, II and III

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Question 4

Which of the following statements regarding deemed distributions is/are TRUE?

I. A participant continues to have an outstanding loan obligation to the plan after a deemed distribution.
II. A deemed distribution is not includable in the gross income of the participant.
III. The participant's account balance is immediately reduced by the amount of the deemed distribution.

A. I only
B. II only
C. I and III only
D. II and III only
E. I, II and III

Question 5

All of the following statements regarding participant loans are TRUE, EXCEPT:

A. Loans must be repaid through payroll deductions.
B. Loans must be adequately secured.
C. Loans must be made according to specific written procedures.
D. Loans must bear a reasonable rate of interest.
E. Loans may not exceed $50,000.

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Question 7

Which of the following statements regarding participant loans is/are TRUE?

I. A plan may include a minimum loan of $1,000.
II. A plan may restrict the availability of loans to parties-in-interest, if desired.
III. The loan may be secured by no more than 50% of the participant's vested accrued benefit.

A. I only
B. II only
C. I and III only
D. II and III only
E. I, II and III

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Question 10

Based on the following information, determine the maximum amount available for a new loan to
Participant A on January 1, 2013:

- Participant A is not a participant in any other plans.
- All required loan payments have been made timely.
- No other loans have been taken during 2012.
- The plan allows for multiple loans.
- The participant has only one loan currently outstanding.

Vested account balance as of 1/1/13, including outstanding loan balance	$51,000
Outstanding loan balance on 1/1/13	$8,500
Outstanding loan balance on 1/1/12	$12,000

A. $13,500
B. $17,000
C. $25,500
D. $29,500
E. $38,000

First limit:
1. Highest outstanding loan in last 12 months = $12,000
2. Current outstanding loan balance = $8,500
3. Lesser of 1 and 2 = $8,500
4. $50,000 less line 3 = $41,500

Second limit:
1. 50% of the vested balance = $25,500
2. Greater of 1 or $10,000 = $25,500

Participant's loan limit:
1.The lesser of the first and second limits = $25,500
2. Current outstanding loan balance = $8,500
3. Current amount available (1 – 2) = $17,000

Question 14

Which of the following statements regarding QDROs is/are TRUE?

I. QDROs must be made pursuant to state domestic relations law.
II. QDROs must include the name and last known mailing address of the plan administrator.
III. QDROs must include the alternate payee's date of birth.

A. I only
B. II only
C. I and III only
D. II and III only
E. I, II and III

Question 15

Which of the following statements regarding hardship withdrawals is/are TRUE?

I. Profit sharing plans are not required to have the same restrictions on hardship withdrawals that are applicable to 401(k) plans.
II. Safe harbor 401(k) contributions may be distributed on account of hardship.
III. Hardship withdrawals may be taken to pay for medical expenses incurred by the participant's beneficiary.

A. I only
B. II only
C. I and III only
D. II and III only
E. I, II and III

401(k) Plans: Testing Part 1

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401(k) Coverage

- Same as PSP: 70% RPT or average benefits test
- Exclusions: 1yr/21; terminatedd less than 500 hours; union; non-resident aliens
- Separate tests for 401(k) and 401(m) = mandatory disaggregation
- Watch terminated exclusion for 401(k) and 401(m) tests- can't exclude terminated less than 500 hours in 401k test

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401(k) Coverage

- 401(k) benefitting = eligible to make deferrals
- 401(m) benefitting = eligible for match (can be conditioned on deferrals)
- 401(m) issue = last day allocation rules

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401(k) Coverage

QNEC - tested as non-elective or as part of 401(k) if used pass ADP

QMAC - either as non-elective or as part of 401(m) if used to pass ACP

Shifted deferrals or match are tested for coverage in their original form: deferrals = 401k test; match = 401m test

401(k) ADP/ACP Test

ADP/ACP test: who is included

ADP:

All eligible EEs, including :

Zero deferrals

Current year terminated employees

Hardship suspension

Okay to exclude irrevocable election and prior year terminees

ACP:

All eligible for match even if zero deferral

ADP/ACP Test: What Is Included

ADP	ACP
• Deferrals • QNEC • Roth • Excess 402(g) for HCEs	• Match • QMAC • After-tax employee contributions • Re-characterized HCE deferral excess

NOT INCLUDED: Catch-up contributions, excess 402(g) for NHCEs, rollovers and employer profit sharing contributions, 415 excess

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401(k) ADP/ACP Test

NHCE Percentage	Maximum HCE Percentage
2% or less	NHCE % × 2
2%–8%	NHCE % + 2
more than 8%	NHCE % × 1.25

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401(k) ADP/ACP Test

ADP/ACP test:

- Current versus prior year testing:
  - Can switch from prior to current in any year BUT subject to double counting limits
  - Current to prior is limited to five-year rule
  - SH plans = current year method
  - Prior year testing = NHCE ADP prior year; HCE ADP current year

401(k) ADP/ACP Test

ADP/ACP test:

- Deemed three-percent rule:
  - New plans only
  - Existing plan that adds 401k or 401m
  - Feature eligible for deemed three percent (considered a new plan)
  - Cannot be increased or decreased

401(k) ADP/ACP Test

ADP/ACP test--passing methodologies

Disaggregated plans testing:

- 1Yr/21 applied regardless of plan eligibility: "disaggregating otherwise eligible EEs"
- Must pass coverage on both groups
- Must run two tests

Early participation testing:

- 1Yr/21 applied regardless of plan eligibility: "disaggregating otherwise eligible EEs"
- Run one test: all HCEs regardless of eligibility included; only include 1yr/21 eligible NHCE EEs

401(k) ADP/ACP Test

Shifting:

Can use with other correction methods

Can shift ADP to ACP to help ACP pass

Can shift fully vested ACP (100% match, QMAC) to help ADP pass

ADP deferrals included in BOTH ADP and ACP

QMACs shifted to ADP ONLY tested in ADP and NOT in ACP

Can shift on a per EE basis (not common)

Watch double-counting!

401(k) ADP/ACP Test

Double counting:

Impacts shifting and switching testing methods but only when switching from current year to prior year

Does not apply to new plans

QNECs from prior year disregarded in current year

QNECs and QMACs that are shifted only count in ONE test

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Question 6

All of the following statements regarding prior year and current year testing methods are TRUE, EXCEPT:

A. Employers are permitted to switch from the prior year testing method to the current year testing method in any subsequent testing year.

B. A safe harbor 401(k) plan is treated as if it were using the current year testing method.

C. Under the prior year testing method, the NHCE ADP for a testing year is the NHCE ADP determined during the prior plan year.

D. Under the prior year testing method, the HCE ADP for a testing year is the HCE ADP determined for the current plan year.

E. Under the prior year testing method, the group of NHCEs included in determining the NHCE.

ADP includes only those participants who are NHCEs as of the current plan year.

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Question 40

All of the following statements regarding the deemed three percent rule are TRUE, EXCEPT:

A. When the deemed three percent rule is used, the three percent may be increased by making QNECs.

B. Plans that use the current year testing method cannot use the deemed three percent rule.

C. A plan may not use the three percent rule if it is a successor plan to a prior 401(k) plan.

D. An existing profit sharing plan that is adding a 401(m) feature is considered a new plan for the deemed three percent rule.

E. An existing profit sharing plan that adds a 401(k) feature is treated as a new plan for the deemed three-percent rule.

Question 41

All of the following statements regarding double-counting limits are TRUE, EXCEPT:

A. Double-counting limits may not apply in the first year of a new plan.

B. Double-counting limits may apply to a plan that uses shifting techniques to satisfy ACP testing.

C. Double-counting limits may apply to a plan that switches from the current year testing method to the prior year testing method.

D. Double-counting limits may apply to a plan that switches from the prior year testing method to the current year testing method.

E. If the double counting limits apply, QNECs used in the prior year must be disregarded in the current year.

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Question 45

All of the following statements regarding shifting techniques are TRUE, EXCEPT:

A. Matching contributions that are subject to a vesting schedule may be shifted to the ADP test.

B. QMACs shifted to the ADP test must be excluded from the ACP test.

C. Designated Roth contributions may be shifted to the ACP test.

D. Shifting may be used in conjunction with other correction methods.

E. All or a portion of the QMACs may be shifted to the ADP test.

Question 46

Which of the following statements regarding shifting techniques is/are TRUE?

I. The elective deferrals of some participants and not others may be shifted to the ACP test.

II. Elective deferrals shifted to the ACP test are not tested in the ADP test.

III. QMACs shifted to the ADP test are not tested in the ACP test.

A. I only

B. II only

C. I and III only

D. II and III only

E. I, II and III

Question 52

All of the following statements regarding coverage testing in a 401(k) plan are TRUE, EXCEPT:

A. When testing the 401(m) component, a participant is considered benefiting if he would be eligible to receive a matching contribution had he made elective contributions.

B. When testing the 401(k) component, terminated participants with less than 500 hours of service are not excluded from the coverage testing group.

C. When testing the 401(m) component, terminated participants with less than 500 hours of service may be excluded from the coverage testing group in some circumstances.

D. All employees who are eligible to make after-tax employee contributions are included in the coverage testing group for the 401(m) plan component.

E. The participants included in the coverage testing group are always the same for the 401(k) and 401(m) components of the plan.

Question 54

All of the following participants must be included in the ACP test, EXCEPT:

A. A participant who is excludable in the minimum coverage tests for the 401(m) component of the plan.

B. A participant who cannot contribute due to a hardship withdrawal taken in the last six months.

C. A participant who would be eligible for a match but elected not to defer.

D. A participant who did not receive a matching contribution due to the annual addition limits under IRC §415.

E. A participant who received a matching contribution but was not employed on the last day of the plan year.

Question 55

Which of the following participants is/are included in the ACP test?

I. Employees eligible to make after-tax employee contributions.

II. Terminated employees eligible to receive matching contributions.

III. Employees eligible to receive matching contributions, but did not make elective contributions.

A. I only

B. II only

C. I and III only

D. II and III only

E. I, II and III

Question 64

Which of the following statements regarding coverage testing in a 401(k) plan is/are TRUE?

I. QNECs are tested as non-elective contributions for coverage purposes.

II. Elective deferrals that are shifted to the ACP test are tested in the 401(k) component of the plan for coverage purposes.

III. QMACs that are included in the ACP test are tested in the 401(m) component of the plan for coverage purposes.

A. I only

B. II only

C. I and III only

D. II and III only

E. I, II and III

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Question 65

Based on the following information, determine the ADP for the following NHCEs:

- Before meeting the eligibility requirements, Employee C made a one-time irrevocable election not to participate in the 401(k) plan or any other plan of the employer.
- Employee E was suspended from deferring during a portion of the plan year because he received a hardship withdrawal.
- The plan satisfies IRC §410(b) coverage requirements.
- All employees listed below have satisfied the eligibility requirements.
- Gross compensation is used in the ADP test.
- None of the employees are catch-up eligible.

A. 3.80%
B. 4.75%
C. 4.88%
D. 6.00%
E. 6.33%

Employee	Gross Compensation	Elective Deferral
A	$50,000	$5,000
B	$40,000	$2,000
C	$30,000	$ 0
D	$20,000	$800
E	$20,000	$0

401(k) Plans: Testing Part 2

401(k) ADP/ACP Test

ADP test -- correction methods

Return $$ to HCEs with interest and attributable match forfeiture (use catch-up limit first)

Leveling method: calculate excess based on percentage then distribute based on $$

Leveling method: test deemed to pass based on $$ distribution

QNEC – pro rata or targeted

QMAC

Re-characterize as after-tax (could cause ACP test problem)

401(k) ADP/ACP Test

ACP test -- correction methods

Return vested $$ to HCEs with interest

Forfeit non-vested match

QNEC or QMAC -- prorata or targeted (but can only be used ONCE for EITHER ADP or ACP)

NOT permitted: suspense accounts, forfeiture of vested matching, failure to allocate

401(k) ADP/ACP Test

ADP/ACP -- corrective distribution rules

Contributions + earnings after 2-1/2 months of plan year end = taxable in current year

Contributions after 2-1/2 months of plan year end = ten percent employer excise tax

Excise tax payable 15 months after PYE on Form 5330

401(k) ADP/ACP Test

ADP/ACP -- corrective distribution rules

- Only occur after the end of the plan year
- Don’t count for RMDs
- Not subject to withholding
- Not subject to ten percent excise tax pre 59-1/2
- HCE can elect Roth or pre-tax OR plan document specifies
- Reported on 1099
- Must be offset by catch-up if plan permits catch-up

ADP QNEC Calculation

Determine HCE Average ADP (ADR)

Determine NHCE ADP (ADR)

QNEC = increased percentage to NHCEs

NHCE compensation * increased percentage

ADP Excess Contribution Calculation

Determine HCE Average ADP (ADR)

Determine NHCE ADP (ADR)

- Excess = Decreased amount for HCEs
- Calculate percentage reduction based on highest HCE deferral percentages
- Take percentage reduction amount and allocate to HCEs with highest deferral contributions

Remember to check attributable match on excess deferral contributions!

Question 42

All of the following statements regarding nondiscrimination testing of otherwise excludable employees are TRUE, EXCEPT:

A. A plan that disaggregates otherwise excludable employees for coverage testing purposes may use the early participation rule for nondiscrimination testing.
B. Only one ADP test is necessary when using the disaggregated plans testing method for nondiscrimination testing.
C. A plan that disaggregates otherwise excludable employees for coverage testing purposes may use the disaggregated plans testing method for nondiscrimination testing.
D. Only one ADP test is necessary when using the early participation rule for nondiscrimination testing.
E. A 401(k) safe harbor plan may be designed so that the safe harbor contribution is available only to statutory employees.

Based on the following information, determine the amount of excess contributions to be distributed to HCE A:

- Gross compensation is used in the ADP test.
- The plan uses the current year testing method.
- None of the participants are catch-up eligible.

Participant	Gross Compensation	Elective Deferrals
HCE A	$150,000	$10,500
HCE B	$100,000	$ 8,000
HCE C	$100,000	$ 6,000
NHCE X	$ 50,000	$ 2,500
NHCE Y	$ 30,000	$ 0
NHCE Z	$ 10,000	$ 700

A. $1,166.67
B. $1,500.00
C. $1,750.00
D. $3,000.00
E. $3,500.00

HCE average ADP = (7 + 8 + 6) / 3 = 7%
NHCE average ADP = (5 + 0 + 7) / 3 = 4%

1.25 * 4% = 5%
OR
2 * 4% = 8%
2 + 4% = 6%

ADP Test Leveling Method

	Compen-sation	Reduced Deferral	Adjusted ADR	Original Deferral Less Reduced Deferral
HCE A	$150,000	$9,000	6%	($10,500 - $9,000) = $1,500
HCE B	$100,000	$6,000	6%	($8,000 - $6,000) = $2,000
HCE C	$100,000	$6,000	6%	($6,000 - $6,000) = $ 0
Total Amount to be Refunded				$3,500

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ADP Test Leveling Method

	Original Deferral	First Reduction	Adjusted Amount	Second Reduction	Adjusted Amount
HCE A	$10,500	($2,500)	$8,000	($500)	$7,500
HCE B	$8,000		$8,000	($500)	$7,500
HCE C	$6,000		$6,000		$6,000

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Question 48

Which of the following statements regarding the corrective distributions of a failed ADP test is/are TRUE?

I. Corrective distributions must not occur until after the end of the plan year.
II. Corrective distributions count towards satisfying the minimum distribution requirements of IRC §401(a)(9).
III. Corrective distributions are subject to the 20 percent mandatory withholding rules.

A. I only
B. III only
C. I and II only
D. II and III only
E. I, II and III

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Question 50

Based on the following information, determine the smallest QNEC to be allocated to all NHCEs to allow the plan to pass the ADP test:

- The QNEC is allocated only to NHCEs in proportion to compensation.
- The plan is not top-heavy.
- The QNEC is the only correction method being used.
- The ADR is the same for the current and prior years.

Participants	Compensation	ADR
HCE1	$100,000	10%
HCE2	$90,000	8%
NHCE1	$50,000	5%
NHCE2	$40,000	5%
NHCE3	$30,000	5%
NHCE4	$20,000	5%

A. $0
B. $2,800
C. $3,080
D. $3,300
E. $4,200

HCE average ADP = (10+8) / 2 = 9%
NHCE average ADP = 5%

NHCE + QNEC = 7%
*2% * (SUM NHCE comp of 140K) =*
$2,800

Question 51

Which of the following statements regarding QNECs is/are TRUE?

I. QNECs may not be conditioned on whether a participant defers under the 401(k) arrangement.
II. QNECs may be used in either the ADP test or the ACP test.
III. QNECs used in the ADP test may not be used in the ACP test.

A. I only
B. II only
C. I and III only
D. II and III only
E. I, II and III

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Question 53

Based on the following information, determine the amount of excess contributions and allocable earnings taxable to the following participant:

- Plan year elective deferrals are $15,000.
- The plan does not allow for designated Roth contributions.
- Plan year excess contributions are $2,000.
- Allocable loss on the excess contribution is ($50).
- Excess contributions and allocable earnings were distributed to the participant within 21/2 months following the end of the plan year.
- The participant is not catch-up eligible.

A. $0
B. $50
C. $1,950
D. $2,000
E. $2,050

Question 57

Based on the following information, determine the maximum elective deferral that HCE 1 could make that would satisfy the ADP test:

- Gross compensation is used in the ADP test.
- None of the participants are catch-up eligible.

Employee	Gross Compensation	Elective Deferral
HCE 1	$100,000	
HCE 1	$50,000	$3,000
NHCE 1	$50,000	$2,000
NHCE 2	$40,000	$1,200
NHCE 2	$30,000	$600

A. $1,500
B. $3,750
C. $4,000
D. $5,000
E. $6,000

NHCE average ADP = (4 + 3 + 2) / 3 = 3%
Max HCE average ADP = 3% + 2% = 5%

(HCE1 + 6%) / 2 = 5%
HCE1 + 6% = 10%
HCE1 = 10% - 6%
*HCE1 = 4% * 100K = $4,000*